No. 12433

IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

FIRST NATIONAL BENEFIT SOCIETY, a corporation,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

PETITIONER'S OPENING BRIEF.

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TOPICAL INDEX

PAGE

Statement of the pleadings 1

Abstract of the case 4

Specifications of errors 6

Argument 7

Conclusion 19

Appendix:

Excerpts from Arizona Revised Code of 1928 ..... App. p. 1

TABLE OF AUTHORITIES CITED

Cases

PAGE

Abilene Ins. Co. v. Commissioner of Int. Rev., 137 F. 2d 191.... 11

American Insurance Co. of Texas v. Thomas, 146 F. 2d 434.... 11, 17

Bowers v. Lawyers Mortgage Co., 285 U. S. 182, 52 S. Ct. 350, 76 L. Ed. 690.... 9

Commissioner v. W. H. Luquire Burial Assn., 102 F. 2d 89.... 9

Commissioner of Int. Rev. v. Ore. Mutual Life Ins. Co., 311 U. S. 267.... 9

Employees of Swift & Co. v. Commissioner, 151 F. 2d 625.... 11

First National Benefit Society v. W. P. Stuart, 134 F. 2d 438.... 14

General Life Insurance Co. v. Commissioner of Int. Rev., 137 F. 2d 185.... 11

General Life Insurance Company v. Commissioner of Int. Rev., 137 F. 2d 191.... 9, 15

Helvering v. Intermountain Life Insurance Co., 294 U. S. 686, 79 L. Ed. 1227.... 9

Helvering v. Oregon Mutual Life Ins. Co., 311 U. S. 267.... 7

Jones v. Oklahoma Benefit Assn., 151 F. 2d 505.... 11

Pioneer Mutual Benefit Association v. Corporation Commission, 123 P. 2d 828.... 13

Weiss v. Stearn, 265 U. S. 242, 44 S. Ct. 490, 68 L. Ed. 1001, 33 A. L. R. 520.... 9

Miscellaneous

Appleman's Treatise on Insurance, Vol. 1, par. 12.... 16

Treasury Department Regulation 94, Articles 201(a)(1) and 203(a) (2)-1 10

STATUTES PAGE

Arizona Benefit Corporation Act of 1937, Sec. 609 (now Sec. 53-609, 1939 Ariz. Code Anno.) 13

Arizona Benefit Corporation Law of 1937, Sec. 607 (now Sec. 53-602, 1939 Ariz. Code Anno.) 16

Arizona Revised Code of 1928, Secs. 607-610 5

Arizona Session Laws of 1937, Chap. 36, Sec. 1, p. 107 (Secs. 53-601 to 53-622, 1939 Ariz. Code Anno.) 1, 3

Arizona Session Laws of 1937, Chap. 36 (now in Chap. 53 of the 1939 Ariz. Code Anno.) 5

Internal Revenue Act, Sec. 201 ..... 3, 5, 8

Internal Revenue Act, Sec. 202 8

Internal Revenue Act, Sec. 203(a) 7

Internal Revenue Act, Sec. 207 ..... 3, 4, 5, 6, 17

Internal Revenue Act, Sec. 207(c)(1)(a) 3, 4, 6

Internal Revenue Act, Sec. 207(c)(3) 3, 7, 17

Internal Revenue Act, Sec. 608b of the 1928 Ariz. Code, as amended in 1937 (Sec. 53-605, 1939 Ariz. Code Anno.) 5, 6

Internal Revenue Act of 1939, Sec. 201(a) 6, 8, 14

Internal Revenue Act of 1939, Sec. 202(b) 15

Internal Revenue Code, Sec. 1141 1

Internal Revenue Code, Sec. 1142 1

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First National Benefit Society, a corporation,

Petitioner,

vs.

Commissioner of Internal Revenue,

Respondent.

PETITIONER'S OPENING BRIEF.

Statement of the Pleadings.

This matter involves a question of Federal Income Taxes and alleged delinquency penalties for the calendar year 1939. The matter was tried in the United States Tax Court under the provisions of Sections 1141 and 1142 of the Internal Revenue Code.

The Petition for Review in the Tax Court sets out the jurisdictional matters as follows:

That the Petitioner is a Corporation duly organized and existing under and by virtue of the laws of the State of Arizona, and during the year 1939 was operating under the provisions of the Arizona Session Laws of 1937, Chapter 36, No. 1, page 107 (Secs. 53-601 to 53-622, 1939 Arizona Code Annotated).

That the return for the period involved was filed with the Collector for the District of Arizona, and that it involved Federal Income Taxes.

Sets forth the Post Office address of Petitioner as 807 West Washington Street, Phoenix, Arizona.

The Petition further states that the amount of the deficiency determined by the Commissioner for $1,135.83 is income taxes for the year 1939, and that the Petitioner's return was filed with the Collector for the District of Arizona and covered its income taxes for the year ending December 31, 1939, and further that a notice of deficiency, a copy of which was attached to the Petition, was mailed to the Petitioner on March 14, 1947.

The Petition to the Tax Court sets out the following Assignments of Errors:

The determination of the tax set forth in said Notice of Deficiency is based on the following errors:

1. The Commissioner determined that compensation due M. C. Reese, accruing under an employment contract, during the year 1939, but not paid during that year was not deductible. Such determination was erroneous for the reason that although Petitioner filed its return on a cash basis, the Commissioner for the purpose of determining Petitioner's taxes for the said year actually accrued claims, where deaths had been reported but were paid during the following year, and this determination leaves the calculation partially on an accrual basis and partially on a cash basis.

2. The Commissioner determined that the sum of $4,518.71 was not deductible from Petitioner's income during the said period. Such determination was erroneous, for the reason that whether Petitioner is to be classi-

fied as a Life Insurance Company under the provisions of Section 201 of the Internal Revenue Act, as it contends, or to be classified as an Insurance Company other than life, under the provisions of Section 207 of said Act, as it is classified by Commissioner it would be entitled to a deduction, even under Section 207 of the Internal Revenue Act as of that year from the net addition required by law to be made within the taxable year to reserve funds. (Sec. 207(c)(1)(A), Internal Revenue Act 1939.)

3. The determination of the deficiency was also in error, for the reason that although he had classified the Petitioner under 207 of the Internal Revenue Act as effective during the year 1939, he did not deduct those funds created by premium deposits, for the payment of expenses and losses as provided in said Section (Sec. 207(c)(3)).

4. The Commissioner erred in his classification of the Petitioner for the reason that the said Petitioner was during the year 1939 a Life Insurance Company, more than fifty per centum of its reserves being held for the fulfillments of its life insurance contracts.

The answer of Respondent admits that the Petitioner is a corporation, organized and existing under and by virtue of the laws of the State of Arizona, and that during the year 1939 was transacting business under and by virtue of the laws of the State of Arizona, Arizona Laws 1937, Chapter 36, No. 1, page 107 [Secs. 53-601 to 53-622, 1939 Ariz Code Anno.), and admits that the return involved herein was filed with the Collector for the District of Arizona and involves Federal Income Taxes.

The Respondent's answer admits the amount of the deficiency the year for which the return was filed, and that the date upon which the notice of deficiency to Petitioner was mailed was March 14, 1947.

The Respondent's answer admits that the Commissioner determined that compensation of M. C. Reese under employment contract during the year 1939 and not paid during that year was not deductible, but denies that it was erroneous.

The Respondent admits that the Commissioner determined that the sum of $4,518.71 was not deductible from Petitioner's income during the said period (the amount deposited with the Arizona State Treasurer for the year 1939), but denies that such determination was erroneous. [Tr. Rec. p. 18.]

The Commissioner's answer further denies that even though classified under Section 207 of the Internal Revenue Act the Petitioner would be entitled to a deduction of the net reserve required by law to be made within the taxable year to reserve funds under the provisions of Section 207(c)(1)(A), Internal Revenue Act of 1939. [Tr. Rec. p. 18.]

The answer also denied that the Commissioner had erred in classifying Petitioner as other than a Life Insurance Company during the year 1939.

The answer further admits that the tax return of Petitioner for the year 1939 was filed on a cash basis and admits that the Commissioner had classified Petitioner under Section 207 of the Internal Revenue Act of 1939, and denies all allegations not specifically admitted.

Abstract of the Case.

The primary issue is, as stated in the memorandum of the Tax Court, whether the petitioner, during the year 1939, was a life insurance company within the provisions of Section 201 of the Internal Revenue Code, or was a mutual insurance company other than life within the meaning of Section 207 thereof.

Further if the Petitioner is to be classified as a mutual insurance company other than life within the meaning of the said Section 207, was the Petitioner entitled to a deduction of $4,518.71 deposited with the Arizona State Treasurer during the taxable year in accordance with the requirements of Section 608b of the 1928 Arizona Code, as amended in 1937 (Sec. 53-605, 1939 Ariz. Code Anno.).

There is also involved the question as to whether if Petitioner is to be classified under the provisions of Section 207 of the Internal Revenue Act of 1939, is it entitled to a deduction of funds received from premiums and held for the payment of expenses and losses, as provided in Section 207(c)(3) of the act.

There is the further question as to whether, since the Commissioner has accrued claims on deaths occurring in 1937 but reported and paid in 1939, the Petitioner would also be entitled to accrue $3,675.41, an unpaid salary claim for the year 1939.

Petitioner was organized under the provisions of Section 607-610 of the 1928 Revised Code of Arizona, but during the year involved in this review was operating under the provisions of Chapter 36, Arizona Session Laws of 1937, now in Chapter 53 of the 1939 Arizona Code Annotated (see index).

The provisions of the 1937 law allowed the companies organized under the prior act to continue in business only on condition that they comply with the provisions of the 1937 act. The questions involved are those pertinent to the matter of income taxation of the Petitioner for the year 1937.

Specifications of Error.

I.

The Tax Court erred in its finding and judgment that Petitioner was not a life insurance company under the provisions of Section 201(a) of the Internal Revenue Act during the year 1939.

II.

The Tax Court erred in its finding and judgment that the Petitioner did not maintain a reserve fund which was held for the fulfillment of its contracts within the meaning of Section 201(a) of the Internal Revenue Act during the year 1939.

III.

The Tax Court erred in its finding and judgment that Petitioner was not entitled to a deduction of $4,518.71 deposited with the Arizona State Treasurer during the taxable year under the provisions of Section 608b of the 1928 Arizona Statutes as amended in 1937 (Sec. 53-605, 1939 Ariz. Code Anno.), as provided in Section 207(c)(1)(A) of the Internal Revenue Act.

IV.

The Tax Court erred in its finding and judgment that Petitioner, if it is to be classified under Section 207 of the applicable Internal Revenue Law, is still not entitled to a deduction of funds held and received during the taxable year for the payment of expenses and losses as provided in Section 207(c)(3) of said act.

V.

The Tax Court erred in its finding and judgment that it was proper for the Respondent to accrue losses on deaths that occurred but were unreported at the end of the taxable year, without accruing unpaid salary claims for the same year.

ARGUMENT.

I.

Referring to Specification of Error No. I.

The Tax Court in its opinion sets out a brief history of the situation taken from *Helvering v. Oregon Mutual Life Ins. Co.,* 311 U. S. 267 [Tr. Rec. pp. 66 & 67], and we believe that a short excerpt from this case will clarify our position in the matter.

The Court in the above case had under consideration the matter of a deduction not of funds held for the fulfillment of its contracts but a deduction from interest earnings under the provisions of Section 203(a) of the Internal Revenue Act (a provision which has during the past two years resulted in exempting from taxation approximately sixty billion in *investment* income of large life insurance companies).

Petitioner is not contending for a deduction from investment income but only for that sum set aside out of premiums paid by policy holders to meet their future claims. However the history of the situation set out by the Court in the *Helvering* case, we believe reveals the purpose of the schedule for taxation of insurance companies, a portion of this statement reads as follows:

> "Legislative history discloses that a deduction similar to that allowed by 203(a) first appeared in the Revenue Act of November 1921. . . . The new plan as it relates to life insurance companies *had as its major objective the elimination of premium receipts from the field of taxable income.* It had long been pointed out to Congress that the receipts except as to a very minor portion of each premium were not true income but were analogous to permanent capital investment."

In enacting legislation with this principle in mind Congress set up a special schedule for the taxation of insurance companies. The enactments in regard to life insurance companies involved in this matter are found in Section 201(a) and Section 202 of the Internal Revenue Act, which during the applicable year read as follows:

> Sec. 201 Tax On Life Insurance Companies.
>
> (a) Definition—When used in this chapter the term "life insurance company" means an insurance company engaged in the business of issuing life insurance and annuity contracts (including contracts of combined life, health, and accident insurance), the reserve funds of which held for the fullfillment of such contracts comprise more than 50 per centum of its total reserve funds.

The tax as applied to such companies is set out in Section 202 of the Internal Revenue Code, as follows:

> Sec. 202. Gross Income of Life Insurance Companies. (a) Gross Income Defined. (1) In General.—In the case of a life insurance company the term "gross income" means the gross amount of income received during the taxable year from interest, dividends, and rents.

The Petitioner was during the year 1939 engaged in the business of life insurance and we do not understand that the Respondent contends that it was in any other business except as he states *"taxwise."*

The general principle in regard to classification of a taxpayer for internal revenue taxation is that the tax-

payer should be classified according to the character of business in which he is engaged.

Bowers v. Lawyers Mortgage Co., 285 U. S. 182, 52 S. Ct. 350, 76 L. Ed. 690;

Weiss v. Stearn, 265 U. S. 242, 44 S. Ct. 490, 68 L. Ed. 1001, 33 A. L. R. 520;

Commissioner v. W. H. Luquire Burial Assn., 102 F. 2d 89.

In enacting a special schedule for life insurance companies Congress surely did not have in mind the granting of special favors to anyone but rather was recognizing the fact that life insurance companies are often engaged in other businesses than that of life insurance.

Where a life insurance company maintains reserves for other purposes than the contingency of death if such reserves such as those held for the endowment features of a contract are larger than those held to fulfill the death claim liability the company is not a life insurance company.

Helvering v. Intermountain Life Insurance Co., 294 U. S. 686, 690, 79 L. Ed. 1227;

Commissioner of Int. Rev. v. Ore. Mutual Life Ins. Co., 311 U. S. 267.

It was not the intention of Congress to give an exemption to any class of companies but rather to lay down a rule for classification according to the business transacted by the taxpayer. In *General Life Insurance Company v. Commissioner of Internal Revenue,* 137 F. 2d 191, the

United States Court of Appeals for the Fifth Circuit said in this regard:

> "It is hardly conceivable that the policy of Congress was to exempt, large, old line, fixed premium life insurance companies, with its risks variedly spread over wide areas, and which had large reserves maintained by interest earnings, from taxation of premium income and to deny the benefit of the exemption, to younger, smaller and weaker life insurance companies with their risks largely localized and which had not yet built up a reserve in the event of serious local epidemics or disasters. To so hold would be to attribute to Congress a misdirected, discrimination in favor of the strong over the weak. To give effect to Treasury Department regulation No. 942 as construed and applied by the Commissioner, would tend to deny the benefits of the exemption to the companies that need it most. It is not thought that this was the intention of Congress."

After the enactment of the law in the form in which it existed in 1939, the Treasury Department enacted its Regulation 94, Articles 201(a)1 and 203(a)(2)-1, which in effect required that the "reserves" set out in the definition must be reserves calculated on an adopted table of mortality or morbidity with an interest element, and that these reserves must be required by state law or by rules of an insurance department under the authority of a state law.

These regulations, in so far as they limit the provisions of the statute and deny the classification as life insurance companies those companies whose reserves are not so calculated or held and required by law, have been held in-

valid by a number of cases. In the following cases companies similar to the Petitioner herein have been held to be life insurance companies:

General Life Insurance Co. v. Commissioner of Int. Rev., 137 F. 2d 185;

Abilene Ins. Co. v. Commissioner of Int. Rev., 137 F. 2d 191;

American Insurance Co. of Texas v. Thomas, 146 F. 2d 434;

Employees of Swift & Co. v. Commissioner, 151 F. 2d 625;

Jones v. Oklahoma Benefit Ass'n, 151 F. 2d 505.

In the *Oklahoma Benefit Life Association* case cited above the United States Appellate Court for the Tenth Circuit held that this company was a life insurance company even though the interest its reserves earned could be used for operating expenses. In that case the Court said in part:

> "It is true that the emergency fund maintained by the Association pursuant to 36 O.S.A. 1941, Par. 701, does not meet the technical requirements of a reserve fund such as is maintained by old line insurance companies. But Congress has never imposed technical requirements, such as actuarial computation, with respect to reserve funds of assessment companies. It is sufficient if it is a fund deposited with the state pursuant to law or maintained under the charter of the company or association exclusively for the payment of claims arising under certificates of membership or policies issued upon the assessment plan and not subject to any other use."

Although dissenting from the majority opinion Judge Huxman agrees with the result arrived at and makes the following statement:

> "The reason for this provision in the statute is quite apparent. Reserve funds do not belong to the company. They are the property of the policyholders. The company is the mere custodian of such funds for the policyholders. As stated by the Fifth Circuit in General Life Ins. Co. v. Commissioner, 137 F. 2d 185, 'In a sense it partakes of the nature of an inchoate trust for the benefit of the policyholders.'"

That the above situation is the case in regard to Petitioner herein we refer to the testimony of the witness M. C. Reese. [Tr. Rec. pp. 30 & 31.]

The witness testified that in March of 1947 the First National Benefit Society "went Legal Reserve." That a stock company was organized out of the expense savings of the Benefit Society and that shares of stock were distributed to each member of the society in proportion to the amount of premium paid by each policyholder, that a $100,000.00 deposit was made with the state treasurer, so that the policy holders of the benefit society are the owners of shares in the Legal Reserve Company in direct proportion to the amount they had contributed to the funds of the benefit society. He testified further that the First National Life Insurance Company has assumed the assets of the benefit society and its liabilities including its tax liabilities.

II.

Referring to Specification of Error No. II.

Section 609 of the 1937 Arizona Benefit Corporation Act (now Sec. 53-609, 1939 Ariz. Code Anno.), provides for a reserve fund. This section has been construed by the Arizona Supreme Court in *Pioneer Mutual Benefit Association v. Corporation Commission,* 123 P. 2d 828, in which the Court held that the requirement of the Arizona Corporation Commission that 50 per centum of of the premiums must be placed in a mortuary fund for the benefit of the company's certificate holders was valid and authorized. The Court said in part:

> "The requirement that such a statement be inserted in all benefit certificates automatically creates a mortuary or reserve fund, because the Legislature certainly did not impose this duty upon a benefit corporation and then permit it to set aside the amount named to that fund provided it saw fit to do so."

And in the same case the Court also said:

> "The Legislature has in the Benefit Corporation law reposed upon the Corporation Commission the duty of seeing to it that the premiums paid for benefit certificates (insurance policies) are sufficient to pay benefit claims."

The words "insurance policies" in parenthesis above are the Court's. It is the gist of this case that the regulations of the Corporation Commission requiring a definite amount of premium to be placed in the mortuary fund for the benefit of the policy holders is valid.

We wish to call the Court's attention to the fact that the requirements of the definition of a life insurance company refer to the amount of fifty per centum of the company's total reserve funds and not to the percentage of premiums allotted to those funds.

In the case of *First National Benefit Society v. W. P. Stuart,* 134 F. 2d 438, the Court in its decision had said that the law of Arizona did not require the maintenance by appellant of any reserve fund; however a petition for rehearing was filed by attorneys for a number of benefit societies who then had pending an appeal to the United States Tax Court, because a portion of the year 1937 was involved in the said suit and the Arizona Benefit Corporation Law had gone into effect during that year. After consideration of the petition the Court entered an order modifying its original opinion as follows:

> "Good cause therefor appearing, It is ordered that the opinion of this court heretofore rendered filed on March 8, 1943, be amended by striking from the first paragraph commencing on page 2 the following sentence: 'The Arizona statutes do not require the maintenance by appellant of any reserve fund.'"

It is the contention of the petitioner therefore that its reserves fulfill all the requirements of the definition enacted by Congress in Section 201(a) of the Internal Revenue Code and that in so far as the Treasury Department regulations add to or limit these requirements they are invalid.

III.

Referring to Specification of Error No. III.

Section 202(b) of the 1939 Internal Revenue Code reads as follows:

> "(b) Reserve Funds Required by Law Defined.—The term 'reserve funds required by law' includes in the case of assessment insurance, sums actually deposited by any company or association with the State or Territorial officers pursuant to law as guaranty or reserve funds, and any funds maintained under the charter or articles of incorporation of the company or association exclusively for the payment of claims arising under certificates of membership or policies issued upon the assessment plan and not subject to any other use."

If Petitioner is not an ordinary life insurance company it would be an assessment life insurance company. In determining this matter with a similar company involved and as to whether the company was an assessment company in relation to the very type of reserves here involved in *General Life Insurance Company v. Commissioner,* 137 F. 2d 185, the United States Court of Appeals for the Fifth Circuit held that although the Articles of Incorporation did not in words provide for the reserves, that the laws of Texas were a part of those Articles, the Court said:

> "Pertinent parts of the law of the state of creation of a corporation are as much a part of its articles of incorporation as if the provisions were expressly written into the articles."

In Appleman's treatise on Insurance Vol. 1, Paragraph 12, the author states that even where advance deposits are fixed and regular premiums collected that if the insurer has the right to call for assessments that such a system is still assessment insurance.

Section 607 of the 1937 Benefit Corporation Law (Sec. 53-602, 1939 Ariz. Code Anno.) provides for corporations, societies or associations where funds are provided by mutual contributions, periodical payments, dues or assessments.

The premium receipts of Petitioner are set up as "dues" and "assessments," the assessments being set up and credited to the mortuary fund.

> See Paragraph 9 of the Stipulation of Facts herein and Petitioner's Exhibit 5 attached thereto [Tr. Rec. p. 53].

All the policies issued by Petitioner to and including the year 1937, contained the following clause:

> "This Corporation is organized as a Death Benefit Society and operating under the provisions of Sections 607, 608, 609, 610 of Chapter XIV of Article 3 of the 1928 Revised Statutes and Amendments of the State of Arizona, and reserves all rights in accordance with law. Annual meeting is held without call at 2 P.M. on the second Saturday of January of each year."

Petitioner should therefore be entitled to a deduction of $4.518.71 deposited with the State Treasurer, during the year 1937, and since these funds were held for the fulfillment of its life insurance contracts as were required by law to be deposited with the State Treasurer for protection of the certificate holders.

IV.

Referring to Specification of Error No. IV.

If Petitioner is to be classified under Section 207, as the Commissioner has classified it, then it would be entitled to a deduction under the provisions of Section 207(c)(3) of the act, which reads as follows:

> "MUTUAL INSURANCE COMPANIES OTHER THAN LIFE AND MARINE. In the case of mutual insurance companies (including interinsurers and reciprocal underwriters, but not including mutual life or mutual marine insurance companies) requiring their members to make premium deposits to provide for losses and expenses, the amount of premium deposits returned to their policyholders *and the amount of premium deposits retained for the payment of losses, expenses, and reinsurance reserves.*" (The emphasis above is ours.)

In the case of *American Ins. Co. of Texas v. Thomas,* 146 F. 2d 434, cited above, the question before the Court was as to this deduction and the majority of the Fifth Circuit Court of Appeals held that this particular company was not a mutual, but held that regardless of that fact, they held that funds set aside for the payment of expenses and losses were not taxable and that they were not income, and that they constituted unearned premiums. In deciding this case the Court said as follows in part:

> "Whatever part of the taxed sums as were derived from insurance premiums and were a part of the increase in the Mortuary Fund of Appellant should have been held to be unearned premiums and deductible from the underwriting income even though the Appellant was not a mutual insurance company."

In a separate concurring opinion Judge Hutcheson said:

> "While I do not agree with the majority that appellant was not a mutual insurance company, I concur in this view that if it was not such company, the sums taxed in each year represented unearned premiums received by an insurance company other than mutual or marine, and were therefore not taxable. While this concurrence reverses the case, I think I should give my reasons for saying that I cannot concur in the conclusion against mutuality. Out of a non-existent and purely imaginary large profit which the managers of the company might make but have not made and apparently will never make, the district judge and my brethren have evoked the specter of a condition which does not exist to deprive appellant of the mutuality it enjoys by statute and in fact."

It would appear therefore that the additions which this Petitioner has made to its reserves held against an ever increasing liability as its policy holders grow older a part of which was required by law to be placed with the State of Arizona, and all of which was required by law to be placed in a Mortuary Fund, that even if these funds constituted no reserve at all, they do constitute money held in trust for the policy holders, contributed by them and belonging to them and held to take care of their future needs. These policy holders paid income taxes on these funds as they acquired them and they now under all decisions in regard thereto constitute, if not technical life insurance reserves, unearned premiums and hence, deductible under the above section.

A considerable portion of these funds also made during the latter part of the year where a six month or annual premium is paid are advanced premiums on risks during the coming year.

V.

Referring to Specification of Error No. V.

The Commissioner should not accrue a portion of the claims against Petitioner and leave unaccrued another claim, unpaid for the sole reason that there were not available funds to pay it.

It is true that the Petitioner filed its income tax return on a cash basis, but each year the Commissioner has accrued the unpaid claims reported at the close of the year but upon which proofs of claim had not been made and then instead of accruing all unpaid claims left unaccrued the unpaid salary claim of M. C. Reese.

It should be noted that during the year 1939, there was transferred from the expense funds of the Petitioner to the mortuary fund the sum of $3000.00 in connection with the salary account although due was not paid in full.

Petitioner therefore contends that the decision of the United States Tax Court should be reversed and the case remanded with instructions to enter judgment for Petitioner.

Respectfully submitted,

ROBERT R. WEAVER,

Attorney for Petitioner.

APPENDIX.

Arizona Revised Code of 1928.

607. Benefit Societies; Limitations. Associations may be formed for the purpose of paying to the nominee of any member a sum upon the death of said member not exceeding three dollars for each member of such association. No such association shall exceed in number, five thousand persons.

608. Formation. Such association shall be formed by filing a verified certificate in the office of the recorder of the county in which the principal place of business is to be situated, and filing a like certificate in the office of the corporation commission; such certificate shall state the general objects of the association, its principal place of business and the names of the officers selected to hold for the first three months, and shall be signed by the said officers and verified by at least three of them.

609. Assessments. Said association, upon the death of any member, may levy an assessment, not exceeding three dollars, upon each living member, and collect and pay the same to the nominee of such deceased, and may also provide for annual assessments upon any one member not to be raised above that established at the time such member joined the association.

610. Powers: Not Controlled by Insurance Laws. Such association may sue and be sued by its name, may loan its funds and own sufficient real property for its business purposes, and such other real property as it may purchase on foreclosure of its mortgages. Such property so obtained through foreclosure shall be sold and conveyed within five years from the day title is obtained, unless the superior court of the proper county shall, upon petition

and good cause shown, extend the time. Such association may make such by-laws as may be necessary for its government and for the transaction of its business, and shall not be subject to the provisions of the general insurance laws.

CHAPTER 36, ARIZONA SESSION LAWS OF 1937.

Section 1. SHORT TITLE. This act may be cited as the benefit corporation law of 1937. (Now section 53-601, Arizona Code, 1939.)

Section 2. Section 607, Revised Code of 1928, is amended to read:

607. BENEFIT CORPORATIONS. Corporations, not for pecuniary profit, may be formed to provide cash benefits for members and cash benefits for the nominees of deceased members, and shall include all corporations, societies and associations operating an insurance business where funds are provided by mutual contributions, periodical payments, dues or assessments, except those hereinafter exempted. (Now section 53602, Arizona Code, 1939.)

Sec. 3. Sec. 608, Revised Code of 1928, is amended to read:

608. FORMATION. (a) Two hundred or more citizens of the United States, residents of this state for at least one year, may form a benefit corporation by filing articles of incorporation, verified by each of them stating the general objects of the corporation, its principal place of business, the time of its commencement and termination, the names of the directors and officers by whom the affairs of the corporation are to be conducted and the time of their election, the corporation's name (which shall indicate its

general character of business and shall not closely resemble the name of any association, life insurance company, or corporation now licensed to do business in this state), and whether private property is to be exempted from liability for the corporate debts. Now Section 53603(a), A. C. 1939.)

(b) When the articles of incorporation have been thus filed and a certified copy thereof recorded in the office of the county recorder of the county in which its place of business is situated, and appointment of a statutory agent filed, the corporation commission shall issue the corporation a certificate of incorporation. (Now section 53-603 (b), A. C. 1939.)

Sec. 4. Article 3, Chapter 14, Revised Code of 1928, is amended by adding section 608a.

608a. Minimum Membership. Such corporation shall have twelve months from the date of its certificate of authority to secure a minimum of not less than five hundred members in good standing. Should the membership at any time fall below said minimum, the corporation shall immediately notify the corporation commission. Within ninety days thereafter, or such further time as the commission may allow, the corporation shall increase its membership to said minimum. If the corporation fails to increase its membership within the time fixed, the commission shall revoke its certificate of authority and thereupon such corporation shall liquidate and dissolve. (Now section 53-604, A. C. 1939.)

Sec. 5. Article 3, chapter 14, Revised Code of 1928, is amended by adding section 608b:

608b. Deposit of Money or Security. (a) Every benefit corporation organized or operating under the pro-

visions of this act, before receiving a certificate of authority to transact business, shall, in addition to the requirements of section 609b, deposit with the state treasurer, to be by him held in trust for the benefit and protection of the corporation's members, the sum of one thousand dollars. Thereafter a further sum of one thousand dollars, divided into twelve equal monthly payments, beginning thirty days after the certificate of authority is issued, shall be likewise deposited with the state treasurer. Failure to pay any such monthly payments shall automatically cancel the corporation's certificate of authority. (Now section 53-605, A. C. 1939.)

(b) In addition to said deposits every such corporation shall, not later than February 1, 1940, and on or before February 1 of each year thereafter, deposit with the state treasurer, to be by him held in trust as hereinafter provided, for the benefit and protection of the members of the corporation, a further sum equal to one dollar for each one thousand dollars of protection in force on December 31 of the preceding year, beginning as of December 31, 1939, until a total of ten thousand dollars has been so deposited. (Now section 53-605(b), A. C. 1939.)

(c) The deposits prescribed by this section shall be subject to withdrawal from the state treasury in whole or in part only on the order of and as directed by the corporation commission, but may, with the commission's approval, be invested in United States or state bonds, which shall be placed with and assigned to the state treasurer and held by him as provided for the original deposits. Subject to approval by the commission any such securities may be exchanged for others of like amounts. The interest on said securities shall be payable to the corporation depositing the same. (Now section 53-605(c), A. C. 1939.)

(d) Any unsettled final judgment of a court of this state shall be a lien on the deposits of money or securities prescribed by section 608b, and subject to execution after thirty days from entry of final judgment. If said deposit is depleted thereby it shall be replenished within ninety days. (Now section 53-605(d), A. C. 1939.)

(e) Said deposit may be considered as a part of any required reserve of the corporation and shall not be subject to withdrawal so long as the corporation has any contract or other liability outstanding. If and when the corporation liquidates, dissolves, or merges with another corporation, and there are no certificates or other liabilities not satisfied or assumed, the deposit shall be returned to the corporation upon the order of the commission, and placed to the credit of the fund from which it was taken or paid to the person who may have advanced it. (Now section 53-605(e), A. C. 1939.)

Sec. ..... Article 3, Chapter 14, Revised Code of 1928, amended by adding section 608c:

608c. Benefit Certificate. (a) Every benefit certificate issued by any such corporation shall specify the maximum amount not exceeding five thousand dollars, on the life of any individual, to be paid on the happening of the contingency therein stated, and shall state the basis or amount to be set aside to the mortuary and reserve fund. The certificate, including any written amendment thereto, and, at the option of the corporation, the application therefor, and the by-laws of the corporation, shall constitute the entire contract between the corporation and the member, and the applicant shall see that all facts required to be stated are set forth in the application. (Now section 53-606(a), A. C. 1939.)

(b) Each corporation shall provide in its certificate for at least fifteen days' grace following the due date of any periodical payment or dues, during which time the certificate shall not be forfeited. If payments are not made according to the terms of the certificate all liability of the member and of the corporation ceases, except as otherwise provided in the certificate. Any corporation may provide for a period of time, which shall be stated in the certificate, for the reinstatement of a lapsed or forfeited certificate, and for a reinstatement fee. If the corporation requires a written application for reinstatement such application shall be the basis of renewing the contract, and any statement made therein may be used by the corporation in defense of its rights under the certificate. (Now section 53-606(b), A. C. 1939.)

Sec. 7. Article 3, chapter 14, Revised Code of 1928, is amended by adding section 608d:

608d. Fidelity Bond. The president, vice-president, or treasurer of every benefit corporation shall furnish a fidelity bond of a company authorized to transact business in the state, in the amount of five thousand dollars, payable to the corporation. (Now section 53-607, A. C. 1939.)

Sec. 8. Article 3, chapter 14, Revised Code of 1928, is amended by adding section 608e:

608e. Liability Limited. The private property of the officers, directors, members, beneficiaries, or employees of any benefit corporation organized under the provisions of this act shall not be liable for the payment of the debts of the corporation. (Now section 53-608, A. C. 1939.)

Sec. 9. Sec. 609, Revised Code of 1928, is amended to read:

609. PAYMENTS AND FUNDS. (a) Every benefit corporation shall provide in its benefit certificate for periodical payments or dues sufficient to pay benefit claims and general operating expenses as stipulated therein. (Now section 53-609(a), A. C. 1939.)

(b) A mortuary and reserve fund, exclusive of other assets, may be created, out of which may be paid all benefit claims arising under the certificates, the deposits required to be made with the state treasurer as provided by section 608b, and attorney's fees and necessary expenses arising out of the defense, settlement, or payment of any contested or disputed claim. The residue of payments made by members, after setting aside the amount required for the mortuary and reserve fund, and interest earned by the assets of the corporation, whether deposited with the state treasurer or otherwise invested, may be used for general operating expenses. (Now section 53-609(b), A. C. 1939.)

Sec. 10. Article 3, chapter 14, Revised Code of 1928, is amended by adding section 609a:

609a. EXAMINATION. At least once in every two years the corporation commission shall require the books and affairs of each benefit corporation to be examined and audited by an accountant designated and commissioned by it, for the purpose of verifying the funds as provided in the benefit certificate thereof. For such purpose the commission and its auditor shall have free access to all books, papers and accounts of the corporation. The cost of any such examination and audit shall be paid by the corporation, but it shall not be required to pay for more than one

such examination and audit in any one year, nor to exceed twenty-five dollars for each one thousand certificates or fraction thereof in force at the time of such examination except that a corporation chartered under the laws of another state shall also pay the traveling expenses of the accountant designated by the commission. All such costs shall be paid upon the completion of the audit or examination. (Now section 53-610, A. C. 1939.)

Sec. 11. Article 3, chapter 14, Revised Code of 1928, is amended by adding section 609b:

Sec. 609b. CERTIFICATE OF AUTHORITY TO TRANSACT BUSINESS. (a) Before any benefit corporation shall solicit applications for benefit certificates it shall file a copy of its certificate with the corporation commission and evidence that it has made the deposit required by section 608c. If the certificate conforms to the requirements of this act, the commission shall within three days issue a written certificate of authority to the corporation to transact business. (Now section 53-611(a), A. C. 1939.)

(b) Upon presentation to the commission of *prima facie* evidence that any benefit corporation is wilfully violating the provisions of this act, the commission shall immediately notify such corporation, stating the manner in which it is alleged the law is being violated. If it appears to the commission that the corporation is continuing such violation, it shall cite the corporation to appear within thirty days to show cause why the alleged violations should not be remedied. If upon said hearing the commission shall find that the corporation is violating the provisions of this act in the particulars stated in the citation, it shall serve a written notice of its decision upon the corporation, which shall be subject to the rights of appeal hereinafter provided. Should the corporation not appeal

from such decision, or if it appeal the appellate court shall uphold the decision of the commission, the corporation shall comply with the order of the commission within ten days thereafter, and upon its failure so to do, the commission may revoke the certificate of authority of such corporation. (Now section 53-611, A. C. 1939.)

Sec. 12. Article 3, chapter 14, Revised Code of 1928, is amended by adding section 609c:

609c. Exemption From Attachment. No money paid or to be paid for any benefit, as provided in a certificate issued by a corporation organized or operating under the provisions of this act, shall be liable to attachment or other process, nor may it be seized, taken, appropriated or applied by any legal or equitable process, nor by operation of law to pay any debt or liability of any member or his nominee, except as may be provided in the benefit certificate. (Now section 53-612, A. C. 1939.)

Sec. 13. Article 3, chapter 14, Revised Code of 1928, is amended by adding section 609d:

609d. Organizations Exempted. The provisions of this act shall not apply to secret or fraternal societies, lodges, or councils, which conduct their business and secure members on the lodge system exclusively, and having a ritualistic work and ceremonies in their societies, lodges, or councils, nor to any mutual or benefit association organized or formed and composed exclusively of members of any such society, lodge, or council, church or religious society, nor to any association of employees employed by one and the same concern, or its subsidiary, nor any labor organization, nor to any life insurance company labor organization, nor to any life insurance company organized or operating under chapter 36, Revised Code of 1928, nor

to any foreign assessment company operating under the general insurance laws of this state. (Now section 53-613, A. C. 1939.)

Sec. 14. Article 3, chapter 14, Revised Code of 1928, is amended by adding section 609e:

609e. No Vested Property Right. No member of a benefit corporation shall have any vested property right or title in any deposits or reserve during the life time of the member, other than as provided in the benefit certificate. (Now section 53-614, A. C. 1939.)

Sec. 15. Sec. 610, Revised Code of 1928, is amended to read:

610. Powers of Benefit Corporations. Any corporation organized under the provisions of this act may contract, sue and be sued by and in its own name, and shall not be subject to the provisions of the general insurance laws, and no law hereafter enacted shall apply to such corporations unless they are expressly designated therein. They may own sufficient real property for their business purposes and such other real property as they may purchase upon foreclosure of their mortgages. Property obtained through foreclosure shall be sold and conveyed within five years from the date title is obtained unless the superior court of the county in which the principal place of business of the corporation is located, shall, upon petition and for good cause shown, extend the time for such sale and conveyance. Such corporation may make and amend necessary by-laws, which shall provide for annual meetings of members who may vote in person or by proxy. The by-laws or the benefit certificate may provide for the qualification of members, mode of acceptance, the fees of admission and periodical payments

or dues, the expulsion of members for non-payment of any periodical payment or dues, the restoration to membership, the employment and compensation of its agents and other regulations not in violation of this act. (Now section 53-615, A. C. 1939.)

Sec. 16. Article 3, chapter 14, Revised Code of 1928, is amended by adding section 610a:

610a. Existing Corporations. Any existing corporations under the provisions of sections 607, 608, 609 and 610, article 3, chapter 14, Revised Code of 1928, shall be deemed to be lawfully incorporated, organized and existing and may continue its corporate existence and transact business under, and avail itself of the provisions hereof without reincorporating or requalifying, except that such corporation shall, on or before January 1, 1938, comply with the provisions hereof as to statutory agent, minimum membership, deposits of money or securities, benefit certificate, fidelity bond, and certificate of authority, and shall be subject to examination as herein provided. (Now section 53-616, A. C. 1939.)

Sec. 17. Article 3, chapter 14, Revised Code of 1928, is amended by adding section 610b:

610b. Foreign Organizations. No benefit corporation, association, or society incorporated or transacting business under the laws of any other state or foreign country, shall transact business in this state until it complies with the requirements of this act. Any person violating any of the provisions of this section shall be guilty of a misdemeanor and upon conviction punished by a fine of not more than five hundred dollars, imprisonment in the county jail for not more than six months, or both. (Now section 53-617, A. C. 1939.)

Sec. 18. Article 3, chapter 14, Revised Code of 1928, is amended by adding section 610c:

610c. FILING FEES. The fees for the filing of instruments and documents pertaining to the organization of benefit corporations shall be the same as the fees provided for filing of like instruments and documents with the corporation commission. (Now section 53-618, A. C. 1939.)

Sec. 19. Article 3, chapter 14, Revised Code of 1928, is amended by adding section 610d:

610d. CONTESTABILITY. (a) All certificates issued by a benefit corporation shall be incontestable after three years from their effective date or three years from the effective date of any reinstatement after lapse, except for non-payment of assessment levied.

(b) To contest the validity of a certificate, or deny liability thereunder, the corporation shall notify the member, or if the member is dead, the beneficiary, by registered letter addressed to such member or beneficiary at the last address known to the corporation. (Now section 53-619, A. C. 1939.)

Sec. 20. Article 3, chapter 14, Revised Code of 1928, is amended by adding section 610e:

610e. APPEAL. Any decision of the corporation commission may, within sixty days after the same has been served on a benefit corporation, be appealed to the superior court of the county in which the principal place of business of such corporation is located. Notice of appeal and a statement of objection to the commission's decision shall be filed with the commission, which shall, within sixty days after the appeal has been filed, transmit a copy of such notice and statement, with a certified copy of the

proceedings before the commission, including a transcript of testimony and all exhibits, to the clerk of the superior court, who shall docket the appeal in the name of the appellant as plaintiff and the corporation commission as defendant. The superior court shall hear such appeal, with or without jury, unless both parties shall file an agreement to a continuance. Either the corporation commission or any such corporation or proposed corporation may appeal from the judgment of the superior court to the supreme court. (Now section 53-620, A. C. 1939.)

Sec. 21. Article 3, chapter 14, Revised Code of 1928, is amended by adding section 610f:

610f. PENALTIES. Any solicitor, agent, examining physician, or other persons who wilfully makes any false or fraudulent statement or misrepresentation in or with reference to any application for benefit or for the purpose of obtaining any money or benefit in or to any corporation transacting business under this act, or any officer of any such corporation who refuses to permit the corporation commission or its auditor to make an examination and audit of the business, books, or records of such corporation, or who wilfully violates any of the provisions of this act shall be guilty of a misdemeanor and upon conviction shall be punished by fine of not more than five hundred dollars, imprisonment in the county jail not more than six months, or both. (Now section 53-621, A. C. 1939.)

Sec. 22. SEVERABILITY. If any provision of this act be held invalid, such invalidity shall not affect other provisions which can be given effect without the invalid provision, and to this end the provisions of the act are declared to be severable. (Now section 53-622, A. C. 1939.)